

HOUSE BUDGET COMMITTEE

Democratic Caucus

The Honorable John M. Spratt Jr. ■ Ranking Democratic Member

B-71 Cannon HOB ■ Washington, DC 20515 ■ 202-226-7200 ■ www.house.gov/budget_democrats

January 26, 2006

CBO Forecasts Continued Large Deficits

Dear Democratic Colleague:

The Bush Administration claims that it is making progress on the deficit, but today the Congressional Budget Office (CBO) released a report that casts doubt on that claim. When the likely funding for our deployments in Iraq and Afghanistan is included, the deficit for 2006 is approximately \$360 billion and the deficit for 2007 is above \$300 billion.

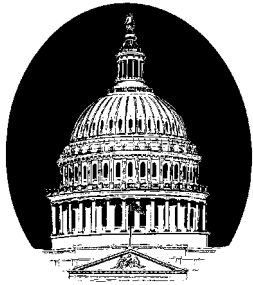
The Bush Administration is accumulating a mountain of debt, a burden for future generations to bear. CBO's estimates show that we will not grow out of these deficits, and far from resolving the problem, the Bush Administration policies make the deficit worse. CBO's projections show the deficit making a decided improvement after 2010, but this results from expiration of the tax cuts passed in 2001, 2002, and 2003 – a policy the Bush Administration clearly does not support.

This year's estimated deficit joins the actual deficits for 2003, 2004, and 2005 to make up the four largest deficits in American history. To accommodate these budgets, the legal debt ceiling of the United States has been raised three times during the Bush Administration and just last month, Secretary Snow wrote Congress urgently seeking a fourth increase.

The House Budget Committee Democratic staff has prepared the attached summary of today's CBO report. It includes information and charts that I hope you will find helpful. Please feel free to contact me or the Democratic staff at 6-7200.

Sincerely,

John M. Spratt, Jr.
Ranking Democratic Member



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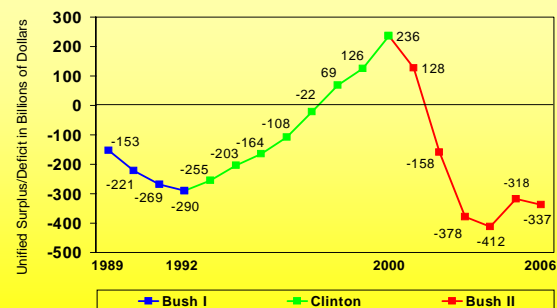
Today's estimates by the Congressional Budget Office (CBO) again remind us of the dramatic fiscal deterioration that has occurred under the Bush Administration. The Administration continues to claim that it is making progress on the deficit, but today's report clearly demonstrates that the Administration's policies continue to make a bad budget situation worse, producing a \$337 billion deficit for 2006 and a \$1.1 trillion deficit over the following five years (2007-2011). The Bush Administration's deficits are producing a mountain of debt that future generations will be burdened with, and just last month Treasury Secretary John Snow had to request the fourth increase in the legal debt limit since 2002.

Triple-Digit Deficits and a Growing Burden of Debt

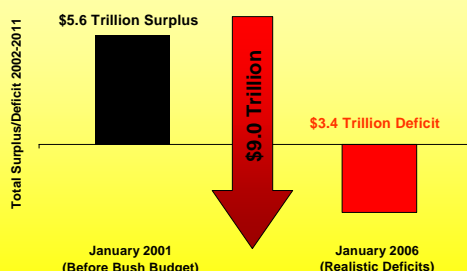
Record Deficits Under Bush Administration — CBO estimates that the deficit for 2006 will be \$337 billion – even before including the cost of an anticipated supplemental appropriation for Iraq and Afghanistan expected early this year. This 2006 deficit is \$19 billion worse than the 2005 deficit of \$318 billion. The deficits for 2003, 2004, 2005, and 2006 are the four largest deficits in American history.

Backsliding Into the Deficit Ditch

From Deficit to Surplus to Deficit Again



Surplus Declines \$9 Trillion Under Republican Policies



Republicans Preside Over Dramatic Fiscal Reversal

— CBO's baseline is required to assume no changes to current policy. When adjustments (described on the next page) are made to the baseline to create a realistic estimate of the current Republican policy agenda, the \$5.6 trillion ten-year surplus (2002-2011) inherited by this Administration in 2001 has been entirely dissipated, and instead replaced by a deficit of \$3.4 trillion over the same time period – a reversal of \$9.0 trillion dollars.

Republicans Increase the Debt Limit by \$3 Trillion

Debt Limit Increases, Billions of Dollars

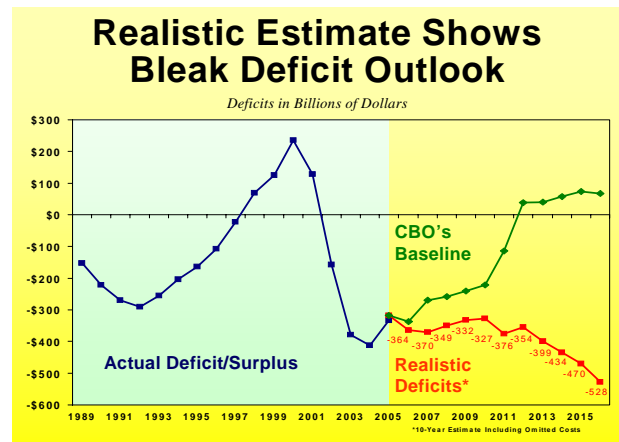
June 2002	\$450
May 2003	\$984
November 2004	\$800
FY2006 Budget Resolution	\$781
Total Increases	\$3,015

Republican Policies Require Another Debt Limit Increase — When this Administration took office in 2001, its first budget estimated that no debt limit increase would be required until 2008. In reality, the Republican Congress has had to enact three debt ceiling increases – totaling \$2.2 trillion – in response to Administration requests. Just last month, Treasury Secretary Snow wrote to Congress to request a fourth such increase. An increase at the \$781 billion level included in last year’s budget resolution would bring the total increases in the debt limit since 2002 to \$3.0 trillion.

More Realistic Forecast Is Even Worse Than CBO Baseline

Realistic Scenario Shows Large Deficits Indefinitely — CBO estimates a ten-year (2007-2016) deficit of \$832 billion, but the Budget Act requires that this baseline estimate must assume no policy changes relative to current law. When realistic adjustments are made to the baseline, this ten-year deficit is actually \$3.9 trillion, triple-digit annual deficits never drop below \$327 billion, and by 2016 the annual deficit rises to \$528 billion.

- To arrive at a realistic forecast, the baseline estimates are adjusted to include the following omitted ten-year costs:
 - ▶ making the President’s tax cuts permanent (\$2.0 trillion, according to CBO);
 - ▶ ongoing operations in Iraq and Afghanistan (\$407 billion, which includes additional outlays of \$20 billion in 2006, according to a scenario estimated by CBO);
 - ▶ fixing the Alternative Minimum Tax (\$864 billion, according to CBO);
 - ▶ the continuation of the President’s defense buildup (about \$296 billion, based on CBO’s re-estimate of the President’s 2006 budget); and
 - ▶ associated interest costs of \$679 billion (using the CBO interest model).
- To produce a realistic forecast, it is also necessary to subtract \$1.0 trillion (including interest costs) over ten years to adjust for the baseline’s required but unrealistic assumption that the supplemental appropriations approved for 2006 will be repeated every year.¹



Illusory “Improvement” Due to Baseline’s Shifting Dates and Incomplete War Funding —

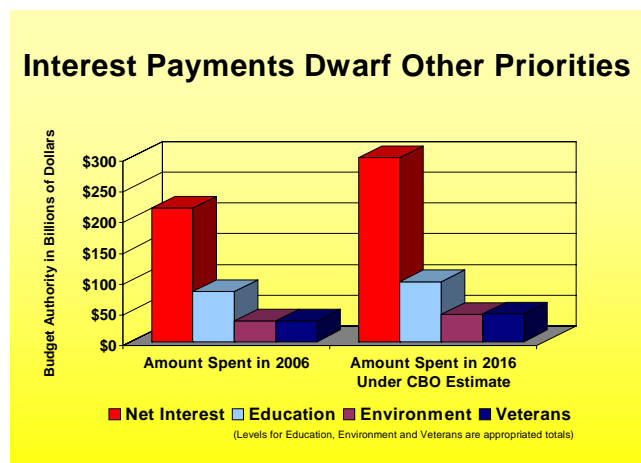
While the ten-year total deficit in today’s document is less than what CBO forecast just five months ago, that “improvement” is due largely to the rules governing how CBO constructs its baseline.

¹ The figures are also adjusted by reducing the estimated deficits by \$105 billion over ten years (CBO’s estimate) to account for the spending reconciliation bill that the Senate has passed and that the House is scheduled to consider on February 1. CBO’s baseline does not include these budget savings.

- First, CBO's August forecast covered the period 2006-2015 while today's covers 2007-2016, thus excluding the estimated 2006 deficit of \$318 billion and including the surplus of \$67 billion projected for 2016. For 2016, CBO assumes that the expensive 2001 and 2003 tax cuts have expired (as they do under current law) because CBO bases its estimates on current law. By excluding a year with a big deficit and instead including a year with a projected (but unlikely) surplus, the ten-year projected deficit artificially appears to improve.
- Second, although the annual funding requirements for the wars in Iraq and Afghanistan have not changed since August, today's baseline includes only about half as much funding for these efforts relative to what was included in the August baseline. Under the rules by which the baseline is constructed, the August baseline reflected the cost of the full year of funding that Congress had already appropriated for Iraq and Afghanistan for 2005, but today's baseline does not, because Congress has so far provided only six months of the funding needed for 2006.

The Harmful Consequences of Deficits

Deficits Mean Wasted Funding on Net Interest — One of the fastest growing parts of the federal budget is the interest paid on the national debt (resulting from the accumulated annual deficits or surpluses). CBO estimates the federal government will pay \$217 billion on a national public debt of \$4.9 trillion in 2006, and that the interest payments will grow by 37.9 percent to \$300 billion in 2016. (With the inclusion of the items omitted from CBO's baseline estimates, the size of these interest payments grows even larger.) These interest payments dwarf the federal investment in many other high-priority areas, including education and training, health care for veterans, and environmental protection. In fact, in a budget constrained by a looming deficit, the government must make its interest payments but has the option – which it exercised this last year – to cut appropriations for these other important services.



Large Deficits Threaten Long-Term Strength of Economy — While the Administration has claimed that record deficits are “manageable,” there is widespread agreement among mainstream economists that large, structural deficits have negative economic consequences. Maintaining such large, persistent deficits results in higher long-term interest rates and a rising national debt, which in turn crowds out private investment and hurts prospects for sustained economic growth. Outgoing Federal Reserve Chairman Alan Greenspan recently warned that if the budget deficits are not reversed, “at some point these deficits would cause the economy to stagnate or worse.”

Chronic Deficits Contribute to Record Trade Deficits — The U.S. current account deficit, a broad measure of the trade balance, has soared under the Bush Administration – increasing from \$389.5 billion in 2001 to \$668.1 billion in 2004 (the most recent annual figures available) – and continues to rise. Structural budget deficits and growing debt exacerbate this problem because

foreign purchases of U.S. debt increase foreign demand for U.S. dollars. This increased demand puts upward pressure on the value of the dollar, which in turn makes U.S. exports more expensive and imports cheaper. Like the budget deficit, the massive trade deficit is considered to be unsustainable.

Republican Claims of Progress Are Unfounded

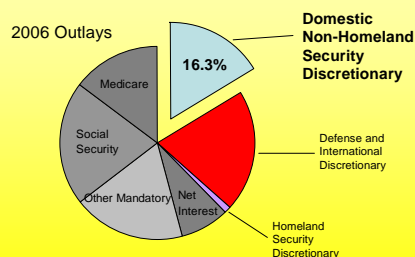
Republican Claims of Progress on Deficit Lack Credibility — Republican claims that progress on the deficit will occur at some future time – including the Administration’s persistent claim that it will cut the 2004 deficit in half by 2009 – lack credibility.

- To begin with, the standard of progress the Administration sets for itself is dubious: turning a record surplus in 2000 into a record deficit by 2004 and then digging only halfway out of that deficit hole hardly constitutes an achievement.
- Moreover, the Administration generates deficit numbers that appear to show modest improvement relative to 2004 by omitting items fundamental to a realistic forecast – such as a repair of the AMT and likely ongoing war costs. When omitted items are included, the realistic 2009 deficit of \$332 billion is even larger than the deficit for 2005, demonstrating that the Administration is not making progress on the deficit.
- Indeed, the Administration’s claim to be cutting the 2004 deficit in half over five years, by 2009, implies that the deficit might be altogether eliminated in a second five years. But the realistic estimates presented here show that, on the contrary, by the end of that second five years, in 2014, the deficit under Administration policies is likely to balloon to \$434 billion.

Republican Reconciliation Plan Makes the Deficit Worse — Next week, the House is expected to consider a spending cut reconciliation bill that Republicans claim will reduce the deficit. In fact, although the bill will have a harmful impact on Americans by reducing spending for Medicaid, student loans, child support enforcement, and other programs, its less than \$40 billion savings over five years will have at most a minor fiscal impact at a time when annual deficits are consistently running at more than \$300 billion. Moreover, the spending reconciliation bill is paired with a tax cut reconciliation bill that will make the deficit worse by more than \$55 billion over five years – thus producing a net *increase* in the deficit from reconciliation of at least \$15 billion.

Deficits Realistically Cannot Be Eliminated by Economic Growth or Appropriations Cuts — Administration claims that deficit problems can be solved through economic growth or cuts in non-defense appropriations are unrealistic and understate the severity of future projected deficits. As former CBO Director Douglas Holtz-Eakin has stated, the nation cannot “grow its way out of

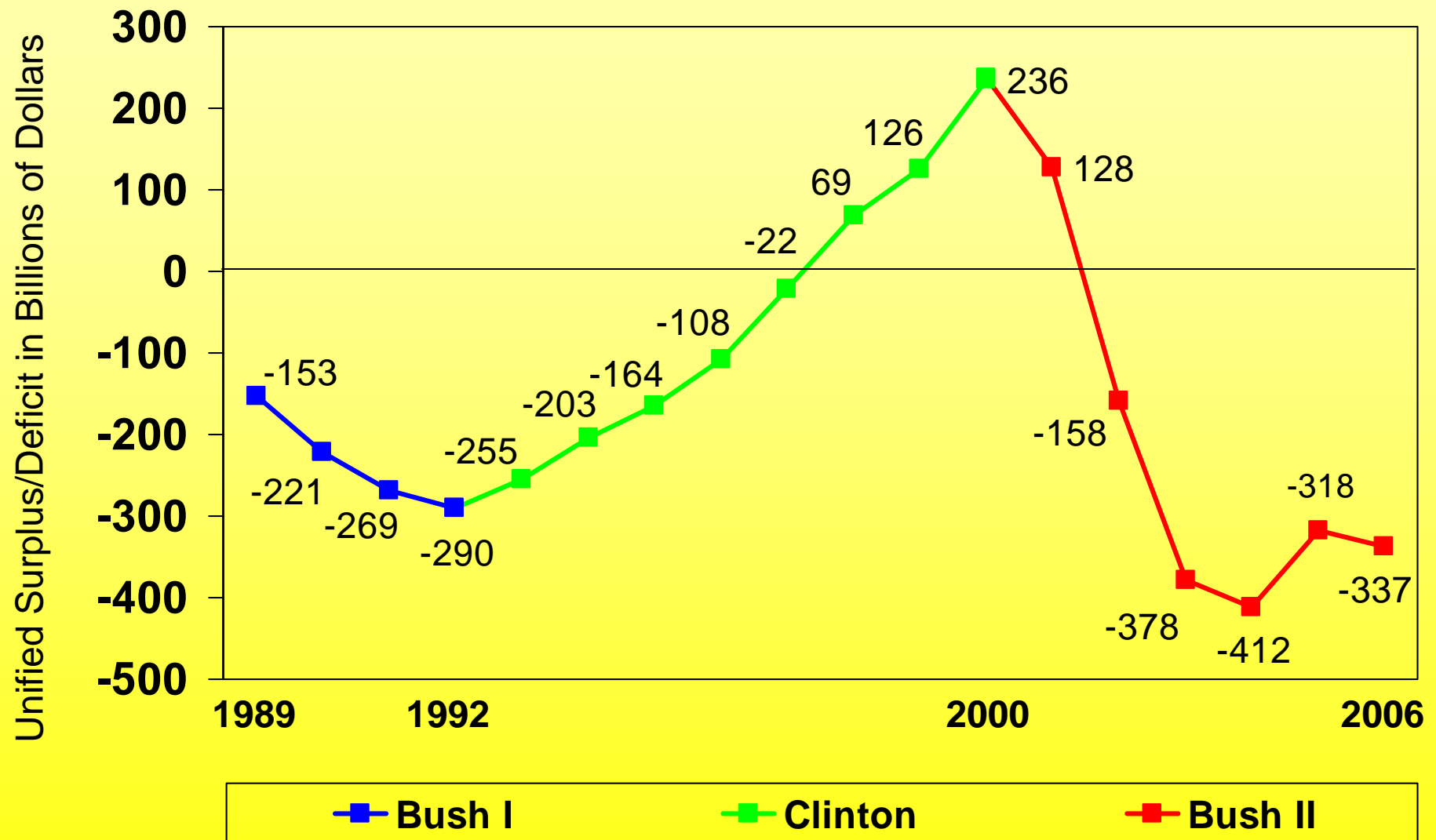
Domestic Non-Homeland Security Funding is Only One-Sixth of Budget



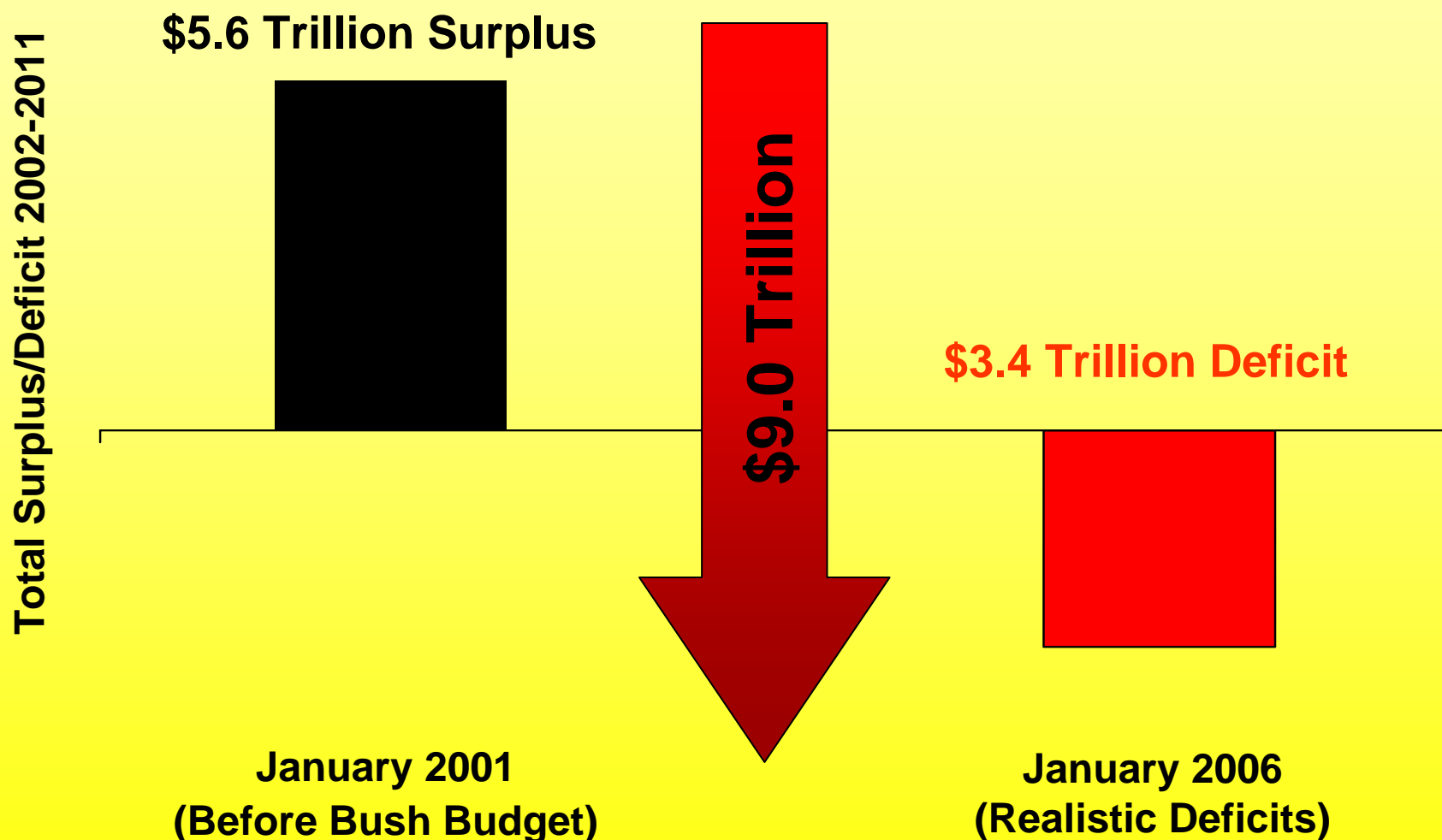
future deficits.” CBO’s forecasts of future deficits already incorporate strong economic growth projections, highlighting the fact that the nation’s fiscal problems cannot simply be solved by solid economic growth. Neither will possible cuts to domestic non-homeland security funding – which accounts for only about one-sixth of the annual budget – make a big dent in the deficit. In fact, total appropriations for domestic services excluding homeland security and emergencies for 2006 is about the size of CBO’s projected 2006 deficit.

Backsliding Into the Deficit Ditch

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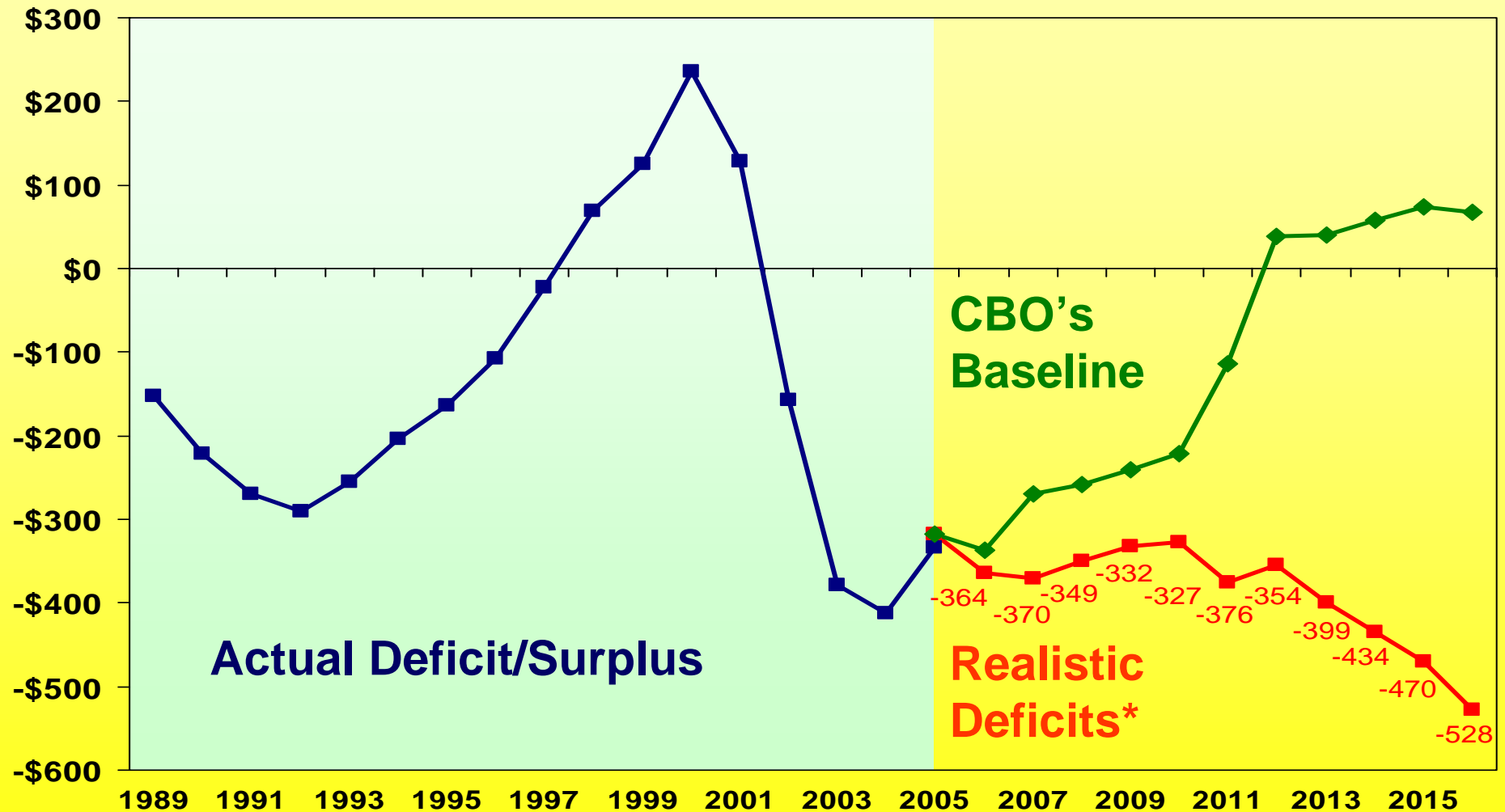


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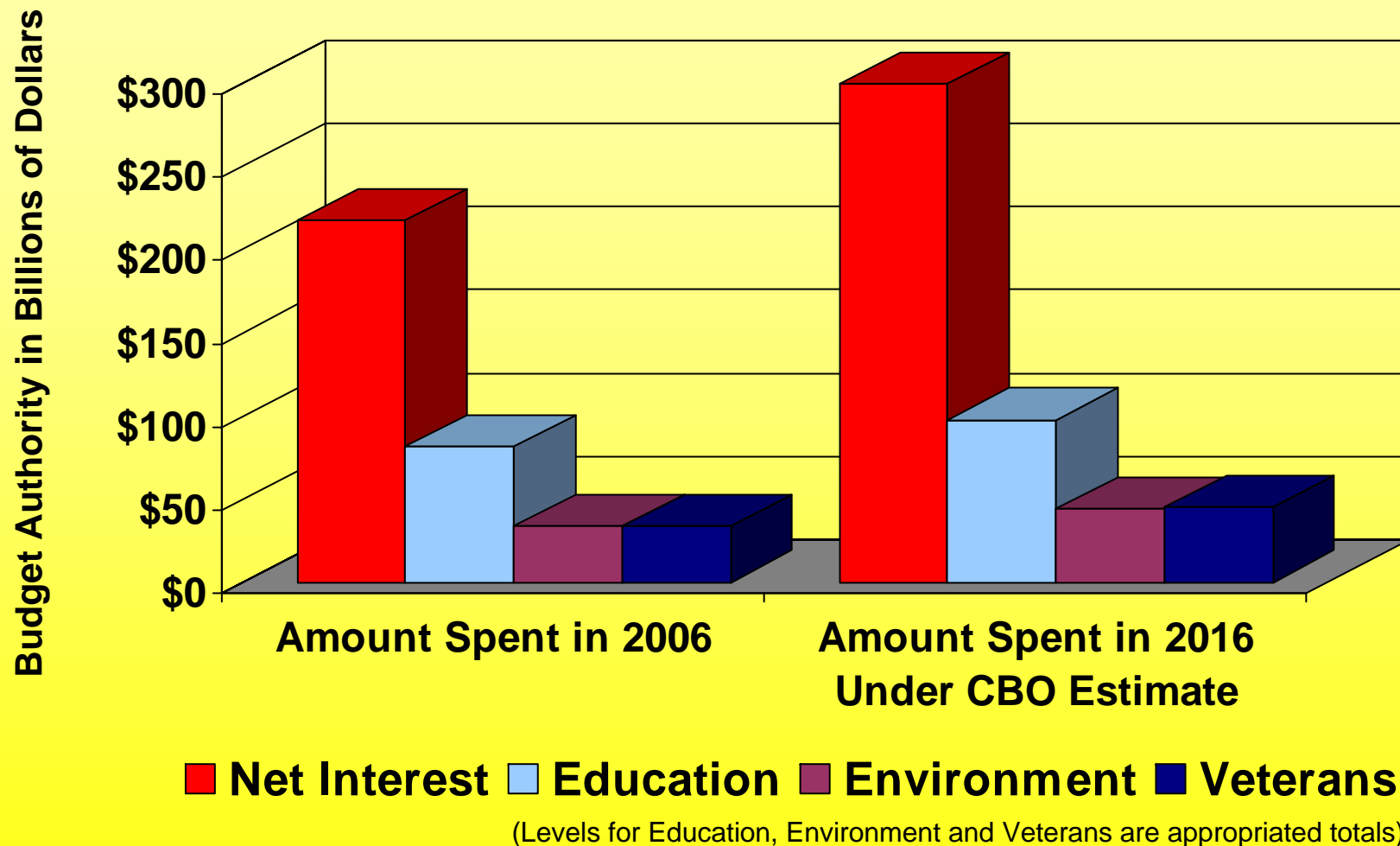
Realistic Estimate Shows Bleak Deficit Outlook

Deficits in Billions of Dollars



*10-Year Estimate Including Omitted Costs

Interest Payments Dwarf Other Priorities

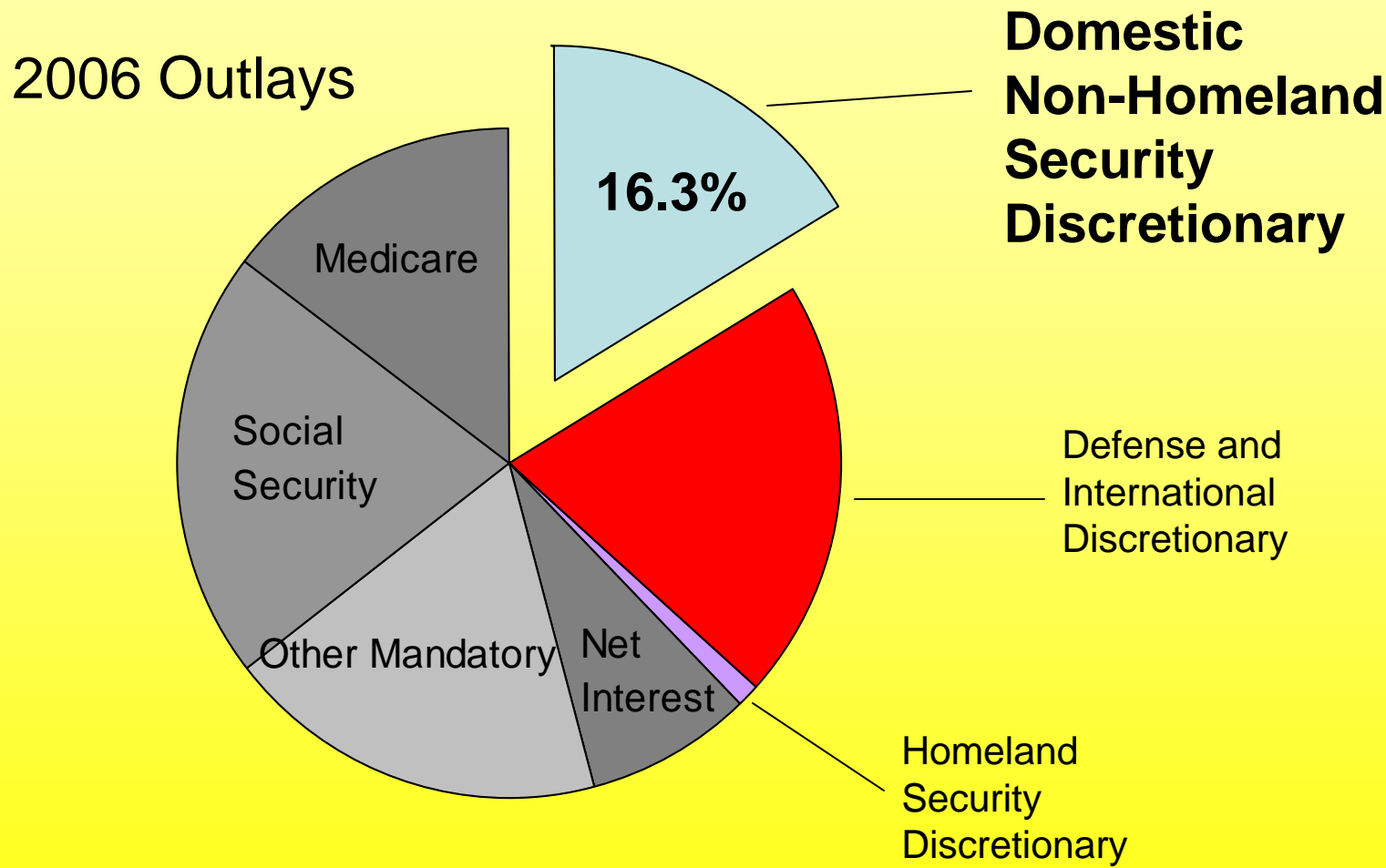


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Debt Limit Increases, Billions of Dollars

June 2002	\$450
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Domestic Non-Homeland Security Funding is Only One-Sixth of Budget



CBO's Budget and Economic Outlook, January 2006

Billions of Dollars	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	Total 2007-2016
CBO Baseline	-337	-270	-259	-241	-222	-114	38	40	57	73	67	-832
Remove Repeating Supplemental	0	43	67	85	95	104	111	119	126	134	143	1026
CBO Baseline w/o repeating supp	-337	-227	-192	-157	-127	-10	148	158	184	207	209	194
Omitted Items												
Extend Expiring Tax Provisions	-6	-18	-31	-49	-53	-195	-302	-319	-335	-347	-362	-2012
Repair AMT	-6	-42	-45	-55	-66	-77	-88	-101	-114	-130	-147	-864
Ongoing Military Operations	-20	-65	-60	-50	-35	-30	-29	-29	-29	-30	-30	-387
Bush Defense Increase	0	-9	-14	-24	-31	-35	-35	-37	-38	-39	-35	-296
Reconciliation Spending Cuts	5	-4	4	21	12	12	14	13	11	11	11	105
Debt Service	-1	-5	-12	-19	-28	-41	-61	-85	-112	-142	-175	-680
Total Changes	-28	-142	-157	-176	-200	-365	-502	-558	-618	-677	-738	-4133
Resulting Deficits	-364	-370	-349	-332	-327	-376	-354	-399	-434	-470	-528	-3939

negative items make deficits worse

Baseline estimates assume tax cuts expire as written in law and 2006 emergency supplemental funding repeats every year and grows with inflation